IN THE

SUPREME COURT OF THE UNITED STATES

No.

APRIL TERM, 1941

KEARNS COAL CORPORATION,
Plaintiff,

v.

UNITED STATES FIDELITY & GUARANTY COMPANY,
Respondent.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

The essential facts have been stated in the petition and we do not repeat them here for reasons of brevity.

Jurisdiction

The jurisdiction of the District Court was based on grounds of diversity of citizenship. Jurisdiction to review the decision of the Circuit Court of Appeals is conferred on this Court by Judicial Code, Section 240A as amended (43 Stat. 938).

Specification of Errors to Be Urged

1. The Circuit Court of Appeals erroneously decided as a matter of law that respondent was not estopped to deny coverage to petitioner under its automobile liability policy (Ex. 1, f. 976).

2. The Court below erred in setting aside the finding of the jury in answer to one of the written interrogatories that petitioner Kearns Coal Corporation was prejudiced or its position was adversely affected by the fact that the respondent, United States Fidelity & Guaranty Company, undertook the defense on petitioner's behalf of the Pasley actions in February 1934 and continued the defense until October 1934, and in holding that this did not form an issue of fact for the jury to determine.

3. The Court below erroneously decided that the liability clauses of the policy operated in connection with the accident to the Pasley boy only for the benefit of the Newton Company and not for that of petitioner.

ARGUMENT

A

The decision of the Court below that as a matter of law respondent was not estopped to deny coverage to petitioner under the policy was contrary to the New York law.

The rule in New York is that where an insurer under a liability policy appears in an action by an injured party on behalf of the insured through its own attorneys and thereby assumes the control of the defense of that action without reservation and with full knowledge of

the material facts, the insurer may not thereafter disclaim liability and is estopped to deny coverage to the insured even where the accident was one not covered by the policy.

In *Rosenbloom* v. *Maryland Cas. Co.*, 153 App. Div. 23, defendant had defended an employee's action for injuries, flowing from a breach of plaintiff's statutory duties, but thereafter disclaimed liability. The court said at page 25:

> "The defense mainly relied upon is that the injury for which Goldstein recovered judgment was not a liability insured against by the terms of the policy. Whether it was or not is perhaps open to question but that question we are not called upon to consider. As has already been said the complaint in the Goldstein case disclosed precisely the nature of his claim and the ground upon which he sought to hold the owners liable, so that when the defendant assumed the defense of the action it had every means of ascertaining whether or not the loss was one for which it was liable under its policy. It is perfectly well settled that under such circumstances, an insurer who has, with full knowledge, undertaken the defense of an action, and deprived the assured of any control of it, will be deemed estopped to deny that the accident was within the terms of the policy."

This rule has been followed and applied in the following decisions of the New York Court of Appeals.

Rosenwasser v. *Globe Indemnity Co.*, 224 N. Y. 561;

Gerka v. *Fidelity & Casualty Co.*, 251 N. Y. 51, 57;

Utterbach Gleason Co. v. *Standard Acc. Ins. Co.*, 193 A. D. 646; affirmed 233 N. Y. 549.

The court below recognizes this to be the rule in New York and other states where the insurer has retained control of the insured's defense to final judgment or to a settlement. It holds, however, that the rule does not apply where the insurer has withdrawn at a time and under circumstances where the insured is left an adequate opportunity to defend. We find no decision which sustains the distinction made by the court below and we do find decisions to the contrary.

In *Sachs* v. *Maryland Cas. Co.,* 170 App. Div. 494, 496, the defendant had originally undertaken the defense of plaintiff in an employee's suit for injuries, but later abandoned the defense, asserting non-liability. Plaintiff took over the defense and successfully defended the action and then sued for his expenses. The insurer defended on the ground that the insured was not liable to the employee and that the accident was not one covered by the policy. The court held defendant liable on the ground that having undertaken the defense and excluded the insured, it could not thereafter assert that the claim was not covered by the policy.

See also:

Miller v. *Union Indemnity Co.,* 209 A. D. 455, 457; affirmed without opinion 240 N. Y. 627;
269 Canal St. Corp. v. *Zurich Co.,* 226 A. D. 516, 518; affirmed without opinion 252 N. Y. 603.

In *Fairbanks Canning Co.* v. *London Guarantee & Acc. Co.,* 154 Mo. App. 327, the insurance company undertook the defense of the negligence action and conducted it for about ten months. It then took the deposition of the plaintiff and his mother and disclaimed before trial on the basis of facts brought out on those depositions. Plain-

tiff took over the defense and negotiated a settlement. The court held that the defendant was estopped to deny coverage.

The cases cited by the court below in support of its position do not sustain it.

In *Lavine* v. *Indemnity Insurance Co. of North America*, 260 N. Y. 399, which is referred to in the opinion as "most nearly analogous" to the case at bar, the record on appeal shows that the summons and complaint in the negligence action were served upon the insured on August 10, 1929, and were received by the defendant insurance company about a week or ten days later. The defendant never appeared nor answered on behalf of the insured in that action and on September 12, 1929, about three weeks after it received the papers in the negligence action, it disclaimed all liability. Defendant's counsel in their brief on appeal stressed the point that defendant had neither appeared nor answered.

The same is true of *Weatherwax* v. *Royal Indemnity Co.*, 250 N. Y. 281, and *Kitsap County Transp. Co.* v. *Pacific Coast Cas. Co.*, 67 Wash. 297, the other cases cited by the court below. In neither case did the insurer appear or answer on behalf of the insured in the negligence action. There was, therefore, no election or agreement to undertake the defense of the action pursuant to the policy, nor any basis for a claim of estoppel by reason of the insurer having undertaken such defense.

Mason-Henry Press v. *Aetna Life Insurance Company*, 211 N. Y. 489, and *Joseph Gordon, Inc.* v. *Massachusetts Bonding Co.*, 229 N. Y. 424, also cited by the court below, are readily distinguishable on the facts. In the *Mason* case the insurer undertook the defense with the express reservation, of which it notified the insured,

that if it developed on the trial that the injured employee was under the legal age of employment the insurance company would not be liable (see opinion pp. 494, 496). In the *Gordon* case there was a similar reservation of rights by the insurer and there was also a deliberate misrepresentation of facts by the insurer. In the case at bar there was no reservation of rights by the insurer and no misrepresentation of the facts by the insured.

The New York decisions above cited which hold that an insurer is estopped to deny coverage to the insured under a liability policy where it has assumed the defense of a personal injuries action on behalf of the insured are based on a familiar theory of estoppel.

In *Rothchild* v. *Title Guarantee & Trust Co.*, 204 N. Y. 458, the rule is stated as follows:

> "When a party with full knowledge, or with sufficient notice of his rights and of all the material facts, freely does what amounts to a recognition or adoption of a contract or transaction as existing, or acts in a manner inconsistent with its repudiation, and so as to affect or interfere with the relations and situation of the parties, he acquiesces in and assents to it and is equitably estopped from impeaching it, although it was originally void or voidable. (Vohmann *v.* Michel, 185 N. Y. 420; 2 Pomeroy's Equity Jurisprudence (3d. ed.) sections 816-821, 965)."

The rule is based on a theory of election. In the most recent case cited above, *Gerka* v. *Fidelity & Cas. Co.*, 251 N. Y. 51, at page 57, the Court of Appeals states, speaking of the insurer:

> "When it proceeded with the defense of the negligence action, with knowledge of its claimed defense under the policy, it made its election and estopped itself from now urging that defense."

The other decisions above cited in support of the rule are to the same effect. The election referred to takes place not after settlement or final judgment, but when the insurance company with full knowledge of the material facts and without reservation assumes the defense of the negligence action on behalf of the insured. It applies, therefore, to the facts in the case at bar.

The question of law thus presented is an important one to that vast army of automobile owners and users who rely upon liability insurance for protection against claims for personal injuries in the event of accident. When an insurance company, after investigation and with knowledge of the circumstances of the accident, undertakes the defense of an action against the insured, the insured is entitled to assume that he will be protected. He loses all control over the conduct of the defense and over any negotiations for settlement. The defense is handled by attorneys employed by the insurance company, in many cases their regular employees, whose personal interest lies primarily with that of the insurance company. If the insurer is to be permitted to conduct the defense through its preliminary stages and then disclaim liability on the basis of facts which were known to it at the time that it assumed control, it may be difficult for the insured to prove actual prejudice where that prejudice nevertheless exists. The decision of the court below stands alone in New York State in holding that there is no resulting prejudice to the insured under such circumstances *as a matter of law*, and no issue of prejudice to be submitted to the jury.

B

There was ample evidence to support the jury's finding that actual prejudice resulted to petitioner from respondent's conduct of the defense of the Pasley action on its behalf.

When the respondent United States Fidelity & Guaranty Company undertook the defense of the Pasley actions on behalf of petitioner, Kearns Coal Corporation, it had already assumed the defense of those actions on behalf of the defendants Newton Contracting Co. Inc., the owner of the truck, and Williams, the driver. At that time it was perfectly apparent to respondent that hostile interests existed as between these three defendants as well as between the two insurance companies. The only way in which the interests of the defendants would cease to be hostile and become similar would be if they were to be covered by the same insurer. Being fully aware of this situation, the respondent nevertheless employed one firm of attorneys to represent all three defendants and one answer was put in on behalf of all three (ff. 448, 452, 1002). This was in itself a representation to petitioner, Kearns Coal Corporation, and its officers, as well as to the attorneys employed by respondent to defend the Pasley action on behalf of the three defendants, that hostility of interest no longer existed and that the respondent intended to cover all three. There is no other theory on which the same attorneys could properly have been employed to carry on a joint defense.

On March 14, 1934, about a month after the appearance on behalf of petitioner had been filed, the attorney for the Pasleys examined the officers of the corporate

defendants before trial, including Mr. Kearns, the president of petitioner. The examination, as stated in the notice, was to be with respect to the operation and control of the truck.

Under the New York decisions it was at that time very doubtful whether any liability on the part of the defendant Kearns Coal Corporation could be established. The Court of Appeals had held in a number of decisions that where a truck and driver are used to deliver coal or some other commodity for another at an hourly or daily rate, they are as a matter of law not under the supervision and control of the person for whom deliveries are being made, but remain in the service of the general employer.

In *Charles* v. *Barrett*, 233 N. Y. 127, one Steinhauser was in the trucking business. He furnished the defendant Adams Express Company with a motor van and chauffeur at the rate of $2 an hour. The defendant did the work of loading at its station and unloading at the railroad terminal. It sealed the van at the point of departure and unsealed it at the point of destination. Between departure and destination the truck remained without interference in charge of the chauffeur. While on such a trip it struck and killed the plaintiff's son. The Court of Appeals affirmed the dismissal of the complaint by the Appellate Division and said at page 129:

> "We think that truck and driver were in the service of the general employer. There was no such change of masters as would relieve Steinhauser of liability if the driver of the van had broken the seals, and stolen the contents. By the same token, there was no such change as to relieve of liability for other torts committed in the conduct of the enterprise. Where to go and when

might be determined for the driver by the commands of the defendant. The duty of going carefully, for the safety of the van as well as for that of wayfarers, remained a duty to the master at whose hands he had received possession. Neither the contract nor its performance shows a change of control so radical as to disturb that duty or its incidence * * *. The rule now is that as long as the employee is furthering the business of his general employer by the service rendered to another, there will be no inference of a new relation unless command has been surrendered, and no inference of its surrender from the mere fact of its division (McNamara v. Leipzig, 227 N. Y. 291; Matter of Schweitzer v. Thompson & Norris Co., 229 N. Y. 97; Meade v. Motor Haulage Co. Inc., 233 N. Y. (527); Driscoll v. Towle, supra)."

See also:

Meade v. *Motor Haulage Co. Inc.,* 197 A. D. 930, affirmed 233 N. Y. 527;

Cattini v. *American Railway Express Co.,* 202 A. D. 336, affirmed 234 N. Y. 585;

Lipshitz v. *Fitzpatrick, Inc.,* 234 N. Y. 592;

Wagner v. *Motor Truck Renting Corp.,* 234 N. Y. 31;

Kellogg v. *Church Charity Foundation,* 203 N. Y. 191;

Hanrahan v. *N. Y. Edison Co.,* 212 A. D. 295;

Moore v. *Stainton,* 80 A. D. 295, affirmed 177 N. Y. 581.

In *Meade* v. *Motor Haulage Co.* (*supra*) the truck and driver owned by defendant were hired by Burns Brothers, retail coal dealers, at $30 per day for use in their business of delivering coal and were engaged in

carrying a load of coal at the time of the accident. The facts in the case do not appear in the official report, but are set forth in the later case of *Cattini* v. *American Railway Express Co.* (*supra*) at page 352 of the opinion.

Under the above decisions it was extremely doubtful whether petitioner would have been liable to the Pasleys even if the accident had happened while the truck and driver were engaged in delivering coal. The non-liability was even clearer in this case in which the truck had made its last delivery and was on its way back to the garage to which it had been directed to return by the general employer, Newton Contracting Co.

> *Bohan* v. *Metropolitan Express Co.*, 122 A. D. 590, 594.

The attorney who represented Kearns Coal Corporation and the other defendants on the examination and who knew that Mr. Kearns was to be examined on the question of supervision and control of the truck at the time of the accident did not advise Mr. Kearns as to the legal status of Kearns Coal Corporation or as to what under the New York decisions legally constituted supervision and control of the truck and driver. Moreover, knowing that Mr. Kearns had not been advised on the law he permitted him, without objection, to answer questions calling for his conclusion on the very question which was to be decided by the court or jury upon the trial, namely, whether the truck and driver were under the supervision and control of Kearns Coal Corporation at the time of the accident.

Mr. Kearns told the truth according to his lights, but he could not have answered correctly the questions put to him on the examination unless he had a correct understanding of the law. Being a layman, he was not familiar

with the decisions above cited and the testimony shows that he understood that if a truck and driver were hired to carry coal for petitioner by the day and he told the driver where he was to take and deliver his load of coal, the truck and driver were under the supervision and control of petitioner, Kearns Coal Corporation, during that day (ff. 593, 595). His testimony on the examination before trial that the truck was under the supervision and control of petitioner at the time of the accident was based on this erroneous understanding of the law.

Moreover, although the questions were objectionable as calling for a conclusion on the part of the witness and an objection as to form could have been made on that ground, the defendant's attorney failed to make any objection. The court below decided that no real prejudice resulted from this failure to object "for it is obvious that the questions could and would have been reframed to elicit substantially the same testimony." The whole purpose of the objection, however, would have been to compel the questions to be asked in proper form and not in a form calling for a conclusion of the witness. When the objection was made to these questions upon the reading of the examination at the trial, the Pasley attorney, Mr. Weltz, argued with considerable force that no objection had been made upon the examination and that if objection had been made he would have asked questions in a different form (ff. 549, 550). If proper objection had been made at the time of the examination, as it should have been, the examination would have brought out the facts and not the witness's erroneous conclusion as to the facts. As a result of this conduct of the examination the attorney for the Pasleys obtained not the facts and circumstances as to the arrangement between Newton and Kearns and as to what the truck and driver were

engaged in doing at the time of the accident on which, under the decisions, no liability on the part of petitioner could have been predicated, but a virtual admission of liability on the part of Kearns Coal Corporation based on an erroneous assumption of supervision and control where supervision and control did not exist, as the jury in this case specifically found.

The reason for this apparent laxity on the part of defendant's counsel on the examination before trial and for his failure to advise Mr. Kearns as to the legal status of petitioner may be traced directly to the respondent's employment of one firm of attorneys to represent all three defendants. Under such circumstances, with the respondent defending on behalf of all defendants, it made no difference under whose supervision and control the truck and driver were at the time of the accident. If any defendant was liable the insurance company had to pay. When the respondent later disclaimed liability to petitioner on the ground of the erroneous conclusion elicited upon this very examination, however, the question whether the truck and driver were under the supervision and control of the petitioner became of vital importance. At that time the damage had been done. Petitioner, or Travelers Insurance Company, if you will, had to defend the action with this damaging and erroneous testimony in the record.

That this testimony was highly damaging there can be no doubt. In fact the jury were entitled to infer that without this testimony of Kearns on the examination before trial no judgment would have been obtained against Kearns Coal Corporation. The court upon the trial of the Pasley action reserved decision on the motions to dismiss at the close of the plaintiff's case and at the close of the entire case (ff. 686, 687) and after the verdict was handed down made the following statement:

> "The Court: I have some doubt as to the propriety of the verdict in connection with the control of this truck, so far as the Kearns Coal Corporation is concerned."

The plaintiff's attorney then urged the testimony of Kearns and Brown on the examination before trial, stating (f. 694):

> "Both of them unequivocally almost in effect stipulated and agreed that the supervision and control at the time of the accident was in the Kearns Coal. There is no question about that."

The Court then asked:

> "Did they say at the time of the accident?"

to which Mr. Weltz replied:

> "Absolutely" (f. 695).

The following request to charge and ruling therein was also made on the Pasley trial (f. 689):

> "Mr. Weltz: I ask your Honor to charge the jury that they have a right to consider in connection with the question of whether the truck was under the supervision of the Kearns Coal Company, the direct testimony of Mr. Kearns in the examination before trial, wherein he admitted that at the time of the accident the truck was under Kearns Coal Company's supervision, together with the other evidence in the case.
>
> The Court: Whatever evidence there is, gentlemen, in the case, you are entitled to take into consideration."

With these facts in the record as to the conduct of the defense of the *Pasley* action while it was under the de-

fendant's control, we contend that a finding that no actual prejudice resulted to petitioner would have been contrary to the evidence. The court below, however, has decided that as a matter of law there was no evidence of prejudice. We submit that this decision is not only in conflict with the local decisions, but constitutes such a departure from the accepted and usual course of judicial proceedings as to call for this Court's exercise of power of supervision.

C

Petitioner was an additional assured under the policy of insurance.

Section II (1) of respondent's policy, which defines the word "assured", provides coverage to one using the insured automobile with the permission of the named assured, or responsible for the use thereof, only in the event that such use was in direct connection with the assured's occupation as expressed in Item 3 of the policy. The truck in question had on the day of the accident (although not at the time of the accident) been carrying coal. The court below decided that such use was not in direct connection with assured's occupation of paving contractor, and concluded that "the liability clauses of the policy operate, in connection with this accident, only for the benefit of the Newton Company, not for that of plaintiff."

The Court overlooked the fact that the agreement to insure the named assured against claims for personal injuries contained in Section I of the policy is likewise limited to injuries sustained by any person or persons "if caused by the ownership, maintenance or use of any

automobile disclosed in the declarations for the purposes therein stated." The purposes stated in the declarations for which the disclosed automobiles were to be used are "commercial" (Item 10) which in turn is defined as the transportation or delivery and the loading and unloading of goods or merchandise in direct connection with the assured's occupation of paving contractor expressed in Item 3.

In other words, if the policy covered the risk at all, it covered Kearns Coal Corporation as well as Newton Contracting Company and Williams. It is true that if the truck was not under the supervision and control of petitioner at the time of the accident, then petitioner could not be held liable. It is likewise true that if Williams was not negligent, Newton Contracting Co. Inc. could not be held liable. The claim was that the truck was being operated by Kearns Coal Corporation at the time of the accident and that Williams was negligent. If this claim was correct, then Kearns Coal Corporation was liable as well as Newton. The agreement in the policy was not only to pay if the assured was liable, but also, Section II(a), "to defend in his name and behalf any suit against the Assured seeking damages on account of such bodily injury or property damage even if such suit is groundless, false or fraudulent." The word "assured" in that section includes an additional assured as well as a named assured.

If the use of the truck to carry coal for Kearns was a "rental to others" within the meaning of the exclusion clause in the policy, or if the use of the truck at the time of the accident was not in direct connection with the insured's occupation as expressed in the policy, in either case this would have excluded coverage of the named assured Newton, as well as the additional assured Kearns.

Respondent knew this and with knowledge of all the material facts undertook the defense of the Pasley actions on behalf of Newton, Williams and Kearns. This constituted an estoppel to deny coverage thereafter, which applied to the additional assured Kearns, as well as to the additional assured Williams or to the named assured Newton. An additional assured stands precisely as a named assured so far as the rights and duties of an insurer are concerned and the rights of an additional assured may be predicated on an estoppel the same as those of a named assured.

> *Sauriolle* v. *O'Gorman,* 86 N. H. 39, 48, 49;
> *Horn* v. *Commonwealth Cas. Co.,* 105 N. J. L. 616;
> *Peterson* v. *Maloney,* 181 Minn. 437, 442.

Coverage itself may be predicated upon an estoppel and an insurance company may be held liable to a named assured or an additional assured because of prejudicial conduct on the part of such insurer, even where the risk involved was specifically excluded under the terms of the policy.

> *General Tire Co.* v. *Standard Acc. Ins. Co.* (C.C.A. 8th Cir.), 65 Fed. (2d) 237, and cases cited under A (*supra*), pp. 15 and 16.

It is needless to speculate as to why respondent chose to extend coverage and undertake the defense of the Pasley actions and not to rest on any claim that the risk was excluded. There was evidence of knowledge on the part of the insurance company at the time the policy was issued that the use of the trucks was not to be limited to the business of paving contractor and the issuance of the certificate of insurance to Stephens Fuel Co., another retail coal dealer, indicated a knowledge that the trucks

were to be used to carry coal for that company. There was no difference in the risk whether coal was carried for Stephens Fuel Company or Kearns Coal Corporation.

Moreover, the meaning of the term "rented to others" is not entirely clear. It was at least doubtful whether it would be held to apply to a case where a truck and driver were used to carry coal for another.

See:

Roadbuilders' Hauling Co. v. *Constitution Indemnity Co. of Philadelphia,* 165 S. C. 363, 366.

The New York Court of Appeals had indicated in a recent decision that the proviso in Section 59 of the New York Vehicle & Traffic Law, which excludes from liability as owner of a motor vehicle under the statute "any person * * * renting or leasing motor vehicles to be operated on the public highway who carries approved liability insurance insuring the renter against liability arising out of his negligence in operating such motor vehicle," does not apply where the automobile, though hired by a third person, is being operated by the servant or employee of the owner.

Atkins v. *Hertz Drivurself Stations, Inc.,* 261 N. Y. 352, 359.

There was also considerable authority, as indicated in the opinion of the Court below, for the Travelers' position that its policy constituted excess insurance. Moreover, respondent did not decide to undertake the defense of Kearns upon receipt of the letter from the Travelers dated February 6, 1934, as stated in the court's opinion. It had agreed to undertake the defense on behalf of

Kearns at the time of the second conversation between Campbell and Dwyer, which was prior to the writing of that letter (ff. 783, 784). At that time, so far as the testimony shows, there had been no discussion or suggestion of any inability to obtain further time to answer or of any possibility of a default.

Respondent undertook the defense of the Pasley action on behalf of petitioner advisedly and in its own interest, because of the possibility that it might be liable to petitioner under the policy. Having waived any questions of exclusion in the case of Newton and Williams, there was no particular reason why it should assert them in the case of Kearns, and by appearing for Kearns it gained exclusive control of the defense. Having deliberately and advisedly and with full knowledge of the facts assumed that defense, it then proceeded so to conduct it as to make it difficult, if not impossible, for Kearns Coal Corporation to successfully defend, where previously it had had an excellent chance of obtaining a dismissal. Having permitted Mr. Kearns, through lack of proper advice and protection, to testify to erroneous conclusions as to the relationship of petitioner to the truck and driver, respondent later disclaimed liability to petitioner, alleging as the ground of disclaimer these same erroneous conclusions. This, under the decisions above cited, it was estopped from doing as a matter of law. At the very least, however, there was a question of fact as to such estoppel, which was properly submitted to the jury, and having been decided by them in favor of petitioner was improperly set aside by the Court below.

Conclusion

We respectfully submit that this case is one calling for the exercise by this court of its supervisory powers in order that the serious and important questions of law which have been decided by the court below contrary to the New York law and in such a manner as to constitute a departure from the accepted and usual course of judicial proceedings may be corrected and properly decided by this court, and that to such end the petition for a writ of certiorari should be granted.

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